

AMENDED IN SENATE JULY 2, 2008
AMENDED IN SENATE JUNE 10, 2008
AMENDED IN ASSEMBLY MAY 19, 2008

CALIFORNIA LEGISLATURE—2007–08 REGULAR SESSION

ASSEMBLY BILL

No. 2738

Introduced by Assembly Member Jones

February 22, 2008

An act to amend Section 2782 of, and to add Sections 2782.9 and 2782.95 to, the Civil Code, relating to indemnity.

LEGISLATIVE COUNSEL'S DIGEST

AB 2738, as amended, Jones. Indemnification: construction contracts.

(1) Existing law provides that, except as specified, all agreements affecting any residential construction contract and amendments to such a contract entered into after January 1, 2008, that purport to indemnify the general contractor or contractor not affiliated with the builder by a subcontractor against liability for claims of construction defects or other injury to property arising from, pertaining to, or relating to the negligence of the nonaffiliated general contractor or nonaffiliated contractor or their other agents, servants, or independent contractors who are directly responsible to the nonaffiliated general contractor or nonaffiliated contractor, or for defects in design furnished by those persons, or for claims that are unrelated to the scope of the work in the agreement, are unenforceable.

A similar provision applies with respect to construction contracts for residential construction entered into after January 1, 2006, that purport to indemnify the builder by a subcontractor against liability for claims of construction defects.

This bill would delete the provisions applicable to construction contracts entered into on or after January 1, 2008, that purport to indemnify the general contractor or contractor not affiliated with the builder. The bill would revise the provisions applicable to contracts entered into after January 1, 2006, to instead apply to contracts entered into after January 1, 2009, and to apply to agreements that purport to insure or indemnify the builder or the general contractor or contractor not affiliated with the builder, as described. The bill would provide that if a builder or contractor tenders a claim, or a portion thereof, to a subcontractor, the subcontractor shall be entitled to *either* defend the claim with counsel of its choice, ~~and the subcontractor shall maintain control of the defense for any claim or portion of claim to which the defense obligation applies.~~ The bill would state the intent of the Legislature with respect to a subcontractor's control of the defense of a claim arising out of the subcontractor's work, the inclusion of violations of functionality standards in a subcontractor's defense and indemnity obligation, and the builder's right to seek equitable indemnity ~~against a subcontractor or pay, within 30 days of receipt of an invoice from the builder or general contractor; no more than a reasonable allocated share of the builder's or general contractor's defense fees and costs.~~ The bill would provide that a builder, general contractor, or subcontractor has the right to seek equitable indemnity for construction defect claims pursuant to these provisions.

(2) Existing law defines a wrap-up insurance policy as an insurance policy, or series of policies, written to cover risks associated with a work of improvement and covering 2 or more contractors or subcontractors that work on the work of improvement.

This bill would provide that all agreements *entered into after January 1, 2009*, for a residential construction project to which a wrap-up insurance policy is applicable which require a subcontractor to indemnify, hold harmless, or defend another for any ~~general liability claim or action, or workers' compensation claim or action,~~ are unenforceable, as specified. The bill would state the intent of the Legislature that, to the extent any contractual provision is deemed unenforceable pursuant to these provisions, any party may pursue an equitable indemnity claim against another party, and that nothing in these provisions shall prohibit a builder or general contractor from requiring a reasonably allocated contribution from a subcontractor or other participant to a self-insured retention or deductible in specified circumstances. The bill would also provide that if an owner, builder,

or general contractor obtains a wrap-up insurance policy or other consolidated insurance program for a work of improvement and requires that any subcontractor provide a credit or compensation for that policy to the owner or original contractor, the credit or compensation required and the coverage provided shall be clearly delineated in the bid documents, and the owner or original contractor may not require that the insured subcontractors under the wrap-up policy credit or compensate the owner or original contractor an amount greater than the amount the owner or original contractor paid to provide that subcontractor coverage under the wrap-up policy.

Vote: majority. Appropriation: no. Fiscal committee: no.
State-mandated local program: no.

The people of the State of California do enact as follows:

1 SECTION 1. Section 2782 of the Civil Code is amended to
2 read:
3 2782. (a) Except as provided in Sections 2782.1, 2782.2,
4 2782.5, and 2782.6, provisions, clauses, covenants, or agreements
5 contained in, collateral to, or affecting any construction contract
6 and that purport to indemnify the promisee against liability for
7 damages for death or bodily injury to persons, injury to property,
8 or any other loss, damage or expense arising from the sole
9 negligence or willful misconduct of the promisee or the promisee's
10 agents, servants, or independent contractors who are directly
11 responsible to the promisee, or for defects in design furnished by
12 those persons, are against public policy and are void and
13 unenforceable; provided, however, that this section shall not affect
14 the validity of any insurance contract, workers' compensation, or
15 agreement issued by an admitted insurer as defined by the
16 Insurance Code.
17 (b) Except as provided in Sections 2782.1, 2782.2, and 2782.5,
18 provisions, clauses, covenants, or agreements contained in,
19 collateral to, or affecting any construction contract with a public
20 agency that purport to impose on the contractor, or relieve the
21 public agency from, liability for the active negligence of the public
22 agency are void and unenforceable.
23 (c) For all construction contracts, and amendments thereto,
24 entered into after January 1, 2009, for residential construction, as
25 used in Title 7 (commencing with Section 895) of Part 2 of

1 Division 2, all provisions, clauses, covenants, and agreements
2 contained in, collateral to, or affecting any construction contract,
3 and amendments thereto, that purport to insure or indemnify,
4 including the cost to defend, the builder, as defined in Section 911,
5 or the general contractor or contractor not affiliated with the
6 builder, as described in subdivision (b) of Section 911, by a
7 subcontractor against liability for claims of construction defects
8 are unenforceable to the extent the claims arise out of, pertain to,
9 or relate to the negligence of the builder or contractor or the
10 builder's or contractor's other agents, other servants, or other
11 independent contractors who are directly responsible to the builder,
12 or for defects in design furnished by those persons, or to the extent
13 the claims do not arise out of, pertain to, or relate to the scope of
14 work in the written agreement between the parties. This section
15 shall not be waived or modified by contractual agreement, act, or
16 omission of the parties. Contractual provisions, clauses, covenants,
17 or agreements not expressly prohibited herein are reserved to the
18 agreement of the parties. Nothing in this subdivision shall prevent
19 any party from exercising its rights under subdivision (a) of Section
20 910. *This subdivision shall not affect the obligations of an*
21 *insurance carrier under the holding of Presley Homes, Inc. v.*
22 *American States Insurance Company (2001) 90 Cal.App.4th 571.*
23 *Nor shall this subdivision affect the obligations of a builder or*
24 *subcontractor pursuant to Title 7 (commencing with Section 895)*
25 *of Part 2 of Division 2.*

26 (d) Subdivision (c) does not prohibit a subcontractor and builder
27 or general contractor from mutually agreeing to the timing or
28 immediacy of the defense and provisions for reimbursement of
29 defense fees and costs, so long as that agreement does not waive
30 or modify the provisions of subdivision (c). ~~However, if a builder~~
31 ~~or contractor tenders a claim, or a portion thereof, to a~~
32 ~~subcontractor pursuant to this provision, the subcontractor shall~~
33 ~~be entitled to defend the claim with counsel of its choice, and the~~
34 ~~subcontractor shall maintain control of the defense for any claim~~
35 ~~or portion of claim to which the defense obligation applies.~~
36 ~~Subdivision (e) shall not affect the obligations of an insurance~~
37 ~~carrier under the holding of Presley Homes, Inc. v. American States~~
38 ~~Insurance Company (2001) 90 Cal.App.4th 571. Subdivision (e)~~
39 ~~shall not affect the builder's or subcontractor's obligations pursuant~~
40 ~~to Title 7 (commencing with Section 895) of Part 2 of Division 2.~~

1 ~~(e) Notwithstanding subdivisions (c) and (d), it is the intent of~~
2 ~~the Legislature to do all of the following:~~

3 ~~(1) Allow a subcontractor to elect whether to control the defense~~
4 ~~of a claim tendered to it by a builder arising out of the~~
5 ~~subcontractor's work, or to participate in funding the builder's~~
6 ~~defense while ensuring a standard for controlling the extent and~~
7 ~~cost of that defense, and to provide a mechanism for imposing~~
8 ~~adverse consequences against subcontractors or their insurers who~~
9 ~~fail to respond to and perform their obligations under a tender.~~

10 ~~(2) Ensure that a subcontractor's defense and indemnity~~
11 ~~obligation includes any violations of functionality standards~~
12 ~~pursuant to standards set forth in Chapter 2 (commencing with~~
13 ~~Section 896) of Title 7 of Part 2 of Division 2 arising out of the~~
14 ~~subcontractor's work.~~

15 ~~(3) Provide that if an attempt by a builder to seek contractual~~
16 ~~defense and indemnity against a subcontractor fails, the builder~~
17 ~~shall have the right to seek equitable indemnity against that~~
18 ~~subcontractor. subject, however, to paragraphs (1) and (2). A~~
19 ~~subcontractor shall owe no defense or indemnity obligation to a~~
20 ~~builder or general contractor for a construction defect claim unless~~
21 ~~and until the builder or general contractor provides a written~~
22 ~~tender of the claim, or portion thereof, to the subcontractor which~~
23 ~~includes all of the information provided to the builder or general~~
24 ~~contractor by the claimant or claimants, including, but not limited~~
25 ~~to, information provided pursuant to subdivision (a) of Section~~
26 ~~910, relating to claims caused by that subcontractor's scope of~~
27 ~~work. This written tender shall have the same force and effect as~~
28 ~~a notice of commencement of a legal proceeding. If a builder or~~
29 ~~general contractor tenders a claim for construction defects, or a~~
30 ~~portion thereof, to a subcontractor in the manner specified by this~~
31 ~~provision, the subcontractor shall elect to perform either of the~~
32 ~~following, the performance of which shall be deemed to satisfy the~~
33 ~~subcontractor's defense obligation to the builder or general~~
34 ~~contractor:~~

35 ~~(1) Defend the claim with counsel of its choice, and the~~
36 ~~subcontractor shall maintain control of the defense for any claim~~
37 ~~or portion of claim to which the defense obligation applies. If a~~
38 ~~subcontractor elects to defend under this paragraph, the~~
39 ~~subcontractor shall provide written notice of the election to the~~
40 ~~builder or general contractor within a reasonable time period~~

1 following receipt of the written tender, and in no event later than
2 90 days following that receipt. Consistent with subdivision (c), the
3 defense by the subcontractor shall be a complete defense of the
4 builder or general contractor of all claims or portions thereof to
5 the extent alleged to be caused by the subcontractor, including
6 any vicarious liability claims against the builder or general
7 contractor resulting from the subcontractor's scope of work, but
8 not including claims resulting from the scope of work, actions, or
9 omissions of the builder, general contractor, or any other party.

10 Any vicarious liability imposed upon a builder or general
11 contractor for claims caused by the subcontractor electing to
12 defend under this paragraph shall be directly enforceable against
13 the subcontractor by the builder, general contractor, or claimant.

14 (2) Pay, within 30 days of receipt of an invoice from the builder
15 or general contractor, no more than a reasonable allocated share
16 of the builder's or general contractor's defense fees and costs, on
17 an ongoing basis during the pendency of the claim, subject to
18 reallocation consistent with subdivision (c), and including any
19 amounts reallocated upon final resolution of the claim, either by
20 settlement or judgment. The builder or general contractor shall
21 allocate a share to itself to the extent a claim or claims are alleged
22 to be caused by its work, actions, or omissions, and a share to
23 each subcontractor to the extent a claim or claims are alleged to
24 be caused by the subcontractor's work, actions, or omissions,
25 regardless of whether the builder or general contractor actually
26 tenders the claim to any particular subcontractor, and regardless
27 of whether that subcontractor is participating in the defense. Any
28 amounts not collected from any particular subcontractor may not
29 be collected from any other subcontractor.

30 (e) Notwithstanding any other provision of law, if a
31 subcontractor fails to timely and adequately perform its obligations
32 under paragraph (1) of subdivision (d), the builder or general
33 contractor shall have the right to pursue a claim against the
34 subcontractor for any resulting compensatory damages,
35 consequential damages, and reasonable attorney's fees. If a
36 subcontractor fails to timely perform its obligations under
37 paragraph (2) of subdivision (d), the builder or general contractor
38 shall have the right to pursue a claim against the subcontractor
39 for any resulting compensatory and consequential damages, as
40 well as for interest on defense and indemnity costs, from the date

1 incurred, at the rate set forth in subdivision (g) of Section 3260,
2 and for the builder's or general contractor's reasonable attorney's
3 fees incurred to recover these amounts. The builder or general
4 contractor shall bear the burden of proof to establish both the
5 subcontractor's failure to perform under either paragraph (1) or
6 (2) of subdivision (d) and any resulting damages. If, upon request
7 by a subcontractor, a builder or general contractor does not
8 reallocate defense fees to subcontractors within 30 days following
9 final resolution of the claim as described above, the subcontractor
10 shall have the right to pursue a claim against the builder or general
11 contractor for any resulting compensatory and consequential
12 damages, as well as for interest on the fees, from the date of final
13 resolution of the claim, at the rate set forth in subdivision (g) of
14 Section 3260, and the subcontractor's reasonable attorney's fees
15 incurred in connection therewith. The subcontractor shall bear
16 the burden of proof to establish both the failure to reallocate the
17 fees and any resulting damages. Nothing in this section shall
18 prohibit the parties from mutually agreeing to reasonable
19 contractual provisions for damages if any party fails to elect for
20 or perform its obligations as stated in this section.

21 (f) A builder, general contractor, or subcontractor shall have
22 the right to seek equitable indemnity for any claim governed by
23 this section.

24 (g) Nothing in this section limits, restricts, or prohibits the right
25 of a builder, general contractor, or subcontractor to seek equitable
26 indemnity against any supplier, design professional, or product
27 manufacturer.

28 (h) As used in this section, "construction defect" means a
29 violation of the standards set forth in Sections 896 and 897.

30 SEC. 2. Section 2782.9 is added to the Civil Code, to read:

31 2782.9. (a) All contracts, provisions, clauses, amendments, or
32 agreements contained therein *entered into after January 1, 2009*,
33 for a residential construction project on which a wrap-up insurance
34 policy, as defined in subdivision (b) of Section 11751.82 of the
35 Insurance Code, or other consolidated insurance program, is
36 applicable, that require a subcontractor to indemnify, hold
37 harmless, or defend another for ~~any general liability claim or action,~~
38 ~~or workers' compensation claim or action,~~ if it is any claim or
39 action covered by that program, arising out of that project are

1 unenforceable. This section shall not be waived or modified by
2 contractual agreement, act, or omission of the parties.

3 (b) It is the intent of the Legislature that, to the extent any
4 contractual provision is deemed unenforceable pursuant to this
5 section, any party may pursue an equitable indemnity claim against
6 another party. The Legislature further intends that nothing in this
7 section shall prohibit a builder or general contractor from requiring
8 a reasonably allocated contribution from a subcontractor or other
9 participant to a self-insured retention or deductible, when and as
10 any such self-insured retention or deductible is incurred by the
11 builder or general contractor, as long as the contribution of
12 subcontractors is reasonably limited.

13 SEC. 3. Section 2782.95 is added to the Civil Code, to read:

14 2782.95. If an owner, builder, or general contractor obtains a
15 wrap-up insurance policy or other consolidated insurance program
16 for a work of improvement and requires that any subcontractor
17 provide a credit or compensation for that policy to the owner or
18 original contractor, then the following shall apply:

19 (a) The credit or compensation required shall be clearly
20 delineated in the bid documents.

21 (b) The coverage provided through the wrap-up insurance policy,
22 including length of time the policy is in effect, shall be clearly
23 delineated in the bid documents.

24 (c) The owner or original contractor may not require that the
25 insured subcontractors under the wrap-up policy credit or
26 compensate the owner or original contractor an amount greater
27 than the amount the owner or original contractor paid to provide
28 that subcontractor coverage under the wrap-up policy.